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IN THE

Supreme Court of the United States

OCTOBER TERM, 1970

No. 619

CONSUMERS POWER COMPANY,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

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WO. 2-8745—WO. 2-8732

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Petitioner, Consumers Power Company, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit, entered in this case on June 5, 1970, and with respect to which a rehearing was denied on July 6, 1970.

OPINIONS BELOW

The Opinion of the United States District Court is reported at 299 F. Supp 1180, and is set forth, in pertinent part, in Appendix A, infra, pages 7-25. The Opinion of the Court of Appeals is reported at ... F. 2d ..., and is set forth in Appendix B, infra, pages 26-30.

JURISDICTION

The Opinion and Judgment of the Court of Appeals was entered on June 5, 1970. A timely Petition for Rehearing was filed June 16, 1970, and was denied July 6, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Is a payment which can be made only to the beneficiary of a retired employee upon the death of such retired employee "deferred compensation" under 26 U.S.C. §404 (a) (5)?

STATUTES INVOLVED

The relevant statutory provisions are set forth in Appendix C, infra, pages 31-32.

STATEMENT

In 1955, Consumers Power Company ("Consumers") entered into an agreement with the Utility Workers of America-CIO, under the terms of which Consumers agreed to pay to the beneficiary of each of its retired employees the sum of $1,000 upon the death of the retired employee. The obligation of Consumers was evidenced by a death benefit certificate delivered to each employee upon his retirement. The benefit was intended as a form of burial insurance for the dependents of the retired employee. No part of the death benefit could be received by the retired employee during his lifetime.

Consumers uses the accrual method of accounting, both with respect to its own books and records and with respect to its Federal income tax returns. The Government admits that the obligation represented by the death benefit certificates is a proper accrual under the rules of Federal income tax accounting as set forth in the Internal Revenue Code and the decisions of this Court.

The Government, while admitting that the unconditional liability represented by the certificates as issued meets all of the normal tests for accrual accounting for Federal income tax purposes, has alleged that the death benefits constitute a plan "deferring the receipt of compensation" within the meaning of §404(a), Title 26, U.S.C..

In the taxable years under consideration by this Court (1955 through 1957), Title 26 U.S.C. §404(a)(5) provided that contributions paid by an employer to a deferred compensation plan are deductible:

> "In the taxable year when paid, if the plan is not one included in paragraph (1), (2), or (3) (not here involved), if the employees' rights to or derived

> from such employer's contribution or such compensation are nonforfeitable at the time the . . . compensation is paid."

On December 30, 1969, the President signed the Tax Reform Act of 1969. §321 of the Act amended §404(a)(5) to read as follows:

> "'OTHER PLANS. If the plan is not one included in paragraph (1), (2), or (3), in the taxable year in which an amount attributable to the contribution is includible in the gross income of employees participating in the plan, but, in the case of a plan in which more than one employee participates only if separate accounts are maintained for each employee."

The District Court held that the death benefit liability did not constitute a plan of deferred compensation, and allowed the liability as a proper accrual for Federal income tax purposes. The Court of Appeals has reversed the District Court, holding that §404(a) controls.

REASONS FOR GRANTING THE WRIT

1. The decision of the Court of Appeals constitutes an unwarranted and basic departure from the principles of Federal income tax accrual accounting, as established by this Court.

2. In view of the action of Congress in amending §404(a)(5), as set forth above, the decision of the Court of Appeals will create for countless employers throughout the United States a situation in which the employers will be unable to deduct death benefit payments for Federal income tax purposes *at any time*, a result which is unconscionable and intolerable for a large class of taxpayers. This question is therefore of major importance in the administration of the tax laws.

ARGUMENT

1. The decision of the Court of Appeals, if allowed to stand, will erode the basic principles of accrual accounting for income tax purposes, as set forth by this Court in a series of decisions over the years. *United States v. Anderson*, 269 U.S. 422 (1926); *Lucas v. American Code Company, Inc.* 280 U.S. 445 (1930); *Lucas v. Ox Fibre Brush Company*, 281 U.S. 115 (1930); *Aluminum Castings Company v. Routzahn*, 282 U.S. 92 (1930); *United States v. Consolidated Edison Company of New York, Inc.*, 366 U.S. 380 (1961). The Government admits that the death benefit liability in this case is a proper accrual under these principles. Nevertheless, the Government's position, as rejected by the District Court, and as adopted by the Court of Appeals, superimposes new and more stringent rules on the basic accrual system of accounting, in a situation which is common to a great many employers throughout the country. The Court of Appeals decision represents a basic, fundamental departure from the long-standing rules of tax accounting.

2. The payment of death benefits by employers to surviving spouses, or other dependents of deceased employees, is a practice followed by many employers throughout the country. Congress has implicitly approved and encouraged this practice by providing, in Title 26 U.S.C. §101(b), that the first $5,000 of such benefits are not to be included in the taxable income of the beneficiaries for Federal income tax purposes.

In the Tax Reform Act of 1969, however, Congress amended §404(a)(5), Title 26, U.S.C. to provide as noted above, that an employer is entitled to a deduction for plans

subject to §404(a)(5) only when the amount attributable to the employer's contribution is includible in the gross income of employees participating in the plan. Since no amount will ever be included in the gross income of employees participating in a death benefit plan, it is clear that if death benefit plans are subject to §404(a), as held by the Court of Appeals in this case, *no employer will ever be able to deduct the amounts he pays the beneficiaries of his retired employees.* This is a result which is so patently unfair and unintended by Congress that it must follow that Congress has never intended §404(a) to apply to death benefits. If the decision of the Court of Appeals is allowed to stand, then not only Consumers, but employers throughout the United States, will find themselves unable to deduct, for Federal income tax purposes, payments which Congress has encouraged them to provide to beneficiaries of deceased employees.

CONCLUSION

For the foregoing reasons, this petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

OPINION AND JUDGMENT OF THE UNITED STATES DISTRICT COURT E. D. MICHIGAN

(Filed March 19, 1969)

Plaintiff brings this action for refund of Federal Income Taxes paid by it for the years 1954 through 1957. The amount sought to be refunded is $1,213,483.06, plus interest. During the years involved herein plaintiff was (and still is for that matter) a public utility engaged in the production, generation, transmission and distribution of electrical energy, and the production, purchase, transmission and distribution of natural gas. It was, and is, subject to the jurisdiction of the Michigan Public Service Commission.

The parties hereto have stipulated to the necessary jurisdictional facts and this Court has jurisdiction herein. The parties have also stipulated that if plaintiff is successful herein they will make the computation of the amounts to be recovered.

The case has been presented to the Court on a Stipulation of Facts, a Supplemental Stipulation of Facts, testimony adduced at the trial and exhibits submitted with the stipulations and those introduced at the trial. The Court also has the benefit of a series of briefs submitted by the parties seriatim. Plaintiff requests findings of fact by the Court in addition to those contained in the stipulation. A copy of the Stipulation of Facts and the Supplemental Stipulation of Facts is appended to this Opinion.

At issue for the Court's determination are three grounds of alleged overpayment of tax by plaintiff for the four years in question. We will deal with each of the grounds

separately. They represent distinct areas. We will refer to them in the same manner as the parties have done—Advertising Expense, Death Benefit and Depreciation—bearing in mind that as to all three, defendant has disallowed or refused to allow deductions in whole or in part to which plaintiff claims it is entitled. Defendant's position is that there has been no overpayment by plaintiff—that plaintiff is not entitled to the additional deductions claimed by it, and that the partial disallowance of certain advertising expense was correct.

* * * * *

Death Benefit

A statement of the issue in the above-captioned area is best given here by drawing upon the plaintiff's own language as it appears in its briefs. We set forth below the factual background, together with plaintiff's argument, in language that is a combination of plaintiff's and the Court's.

> The death benefit issue involves the amount deductible for Federal Income Tax purposes during each of the taxable years 1955, 1956 and 1957. The plaintiff claims that all events had occurred by the end of each of these years to establish the fact of its liability to its retired employees (as a result of the issuance of Death Benefit Certificates to these employees), and that the amount of such liability could be determined with reasonable accuracy.
>
> Prior to the year 1955 the plaintiff provided death benefit payments usually in the amount of $1,000, to the beneficiaries of its retired employees upon the death of such retired employees. This death benefit program was insured and the plaintiff's premium

payments to the insurance company were allowed as a deduction for income tax purposes by the defendant. Starting in 1955 the plaintiff continued its death benefit program, but changed the method of financing to that of a self-insured plan.

Plaintiff claims:

That the death benefit certificate unconditionally obligated the plaintiff to pay the death benefit upon the occurrence of an event which was certain to happen —the death of the retired employee— and that, therefore, on the last day of each of the years, 1955, 1956 and 1957, the plaintiff had an actuarially determined obligation to pay death benefits on account of those employees already retired and to those employees to be retired in the future;

that this obligation with respect to plaintiff's retired employees was fixed and vested and could only be discharged by payment of the death benefit upon the employee's death; and,

that it is entitled to deduct at least the face amount of the certificates it delivered to retiring employees each year.

Plaintiff has placed in the record an actuarial determination of the present value of the outstanding certificates at the end of each year to be used if it be determined that the plaintiff would be entitled to a deduction equal to the present value of the delivered certificates, and contends that it should be entitled to deduct in each of the years 1955, 1956 and 1957 an amount equal to the annual increase in present values of the Death Certificates delivered and outstanding.

The plaintiff's Death Benefit Plan arose out of a labor dispute with its Union employees and the recommenda-

Special Commission under the Michigan Labor Act that the parties agree to a contract provi- by the Company provides life insurance or ...fits of $1,000 for all retired or retiring employ- ... agreement was adopted by the Union and Com- ...September 20, 1955, and provides in part as fol- ...

... full time regular employee who works to or ... Normal Retirement Date on or after March ... will be included in the Plan." [Sec. II, par. 1]

... eligible employee will be permitted to desig- ... payee or payees of the Benefit and in the ab- ... of such designation the Benefit shall be payable ... estate. [Sec. III, par. 1]

... eligible employee on retirement will be given ...tificate by the Company indicating his eligibility ... Benefit under the Plan.

...yment of Benefits will be made by the Company ...ceipt of a properly executed claim form signed ... designated payee or payees and accompanied ...certified copy of the Death Certificate of the de- ... retired employee. [Sec. V, pars. 1, 2.]"

...spect to the contentions of defendant we set them ...w in the language of its briefs, in combination ... of our own language:

...fendant contends that there are three issues pre- ... the plaintiff's claim for deductions in 1935, ... and 1957 of accrued liabilities under its Death ...t Plan, as follows: (1) Whether, under Section ... of the Internal Revenue Code of 1954, the

plaintiff is entitled only to the deduction of the benefits actually paid during the year, which it claimed and was allowed on its return; (2) whether, if Section 404 (a)(5) is not applicable, the plaintiff was otherwise entitled to a greater deduction; and (3) the proper amount of any greater deduction.*

Re Section 404(a)(5) the defendant contends:

That Section 404(a)(5) requires that regardless of other rules of accounting, compensation paid or accrued on account of any employee under a plan de-

* Section 404 of the Internal Revenue Code of 1954, 26 U.S.C., 1964 ed., provides:

"a) General Rule.—If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under section 162 (relating to trade or business expenses) or section 212 (relating to expenses for the production of income); but, if they satisfy the conditons of either of such sections, they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year:

(1) Pension trusts.—In the taxable year when paid, if the contributions are paid into a pension trust, and * * * the trust is exempt under section 501(a) * * *.

(2) Employees annuities.—In the taxable year when paid * * * if the contributions are paid toward the purchase of * * *.

(3) Stock bonus and profit-sharing trusts.—* * * In the taxable year when paid, if the contributions are paid into a stock bonus or profit-sharing trust, and * * * the trust is exempt under section 501(a) * * *.

* * * * *

(5) Other plans.—In the taxable year when paid, if the plan is not one included in paragraph (1), (2), or (3), if the employees' rights to or derived from such employer's contribution or compensation are nonforfeitable at the time the contribution or compensation is paid. * * *"

ferring the receipt of such compensation is deductible only in the taxable year when such compensation is actually paid to the employee or his beneficiary;

that Section 404(a)(5) excises such arrangements as the plaintiff's from the normal rules of tax accounting, regardless of whether the taxpayer is on a cash, accrual or other method of accounting;

that a deduction is allowable only in the year of payment, and then only if the employee's rights are nonforfeitable;

that, therefore, the defendant holds that the commuted value of the unpaid balance of the obligation was not deductible before its actual payment;

that Section 404(a)(5) is an application of the long-standing rule designed to forestall tax avoidance, that compensation to be paid in the future on account of an employee must be irrevocably set aside by an employer before it is deductible. Compensation is paid, within the meaning of Section 404(a)(5), at the time the funds are paid or made available to the employee. With respect to that section, which was adopted without change from the 1939 Code, the House Committee Report on the 1954 Code further stated that "[t]he employer cannot take a deduction when he makes his contribution unless the benefits are immediately paid to the employee." (H. Rept. No. 1337, 83d Cong., 2d Sess., pp. 43-44);

that plaintiff's Death Benefit Plan originated in collective bargaining between plaintiff and its employees' Union, regardless of whether or not the plaintiff considers it merely burial insurance for the family;

that as death benefits, plaintiff's payments clearly were compensation paid on account of any employee under a plan deferring the receipt of such compensation;

that Treasury regulations on Income Tax (1954 Code) expressly provides that "Section 404(a) also governs the deductibility of unfunded pensions and death benefits paid directly to former employees or their beneficiaries" (Sec. 1.404(a)-1 (a) (1), 26 C.F.R. Sec. 1.404(a)-1(a) (1)), and that "if amounts are paid as a death benefit to the beneficiaries of an employee (for example, by continuing his salary for a reasonable period), * * * such amounts are deductible under section 404(a) (5) in any case when they are not deductible under the other paragraphs of section 404 (a)." (Sec. 1.404(a)-12, 26 C.F.R. Sec. 1.404(a)-12);

that plaintiff's contention that Section 404(a)(5) is limited to benefits received by the employee during his life is refuted by the statute itself which speaks of "compensation paid or accrued on account of [not 'to'] any employee";

that regardless of whether from the institution of its Death Benefit Plan in 1955, or after an employee's retirement at or after the age of 65, or only after the retired employee's death, the plaintiff became obligated to pay the benefit to the employee's beneficiary, the plan was a plan deferring the receipt of such compensation and under Section 404(a) (5) the benfit was deductible by the plaintiff only when the plaintiff actually paid it to the beneficiary.

The question as to what is and what is not deferred compensation cannot be stretched to include any consideration of the Death Benefit Plan of plaintiff. Nor do the provisions

of Section 162 and/or 212 of the Internal Revenue Code have any affinity for the plaintiff's Death Benefit Plan so as to place the plan within the "catch-all" provisions of Section 404(a) (5). *John C. Nordt Co.*, 46 T.C. 431, 441, states that:

> "Section 404(a)(5) is a 'catch-all provision' intended to cover plans which do not fall in to the formal categories (such as pension trusts, employees' annuities, and stock bonus and profit-sharing trusts) described in paragraphs (1), (2), and (3) of subsection (a). * * *"

No testimony was adduced in this proceeding that in any way associated plaintiff's Death Benefit Plan with a continuance of the salary of any retired employee of Consumers for *any* period of time, reasonable or otherwise. It is conceded by defendant, and it is readily apparent, that plaintiff's Death Benefit Plan evolved from an "arm's length transaction" between the Company and the employees' Union, upon the recommendation of a Special Commission appointed by the Governor of the State of Michigan under the Michigan Labor Mediation Act (Act 176 of Public Acts of 1947). The Special Commission's primary function was to aid management and labor, through the process of mediation, in reaching amicable settlements of labor disputes then pending between the employees' Union and the plaintiff. This recommendation by the Special Commission produced the following resolution (adopted September 22, 1955, here as Exhibit CC, by the Board of Directors of Consumers Power Company:

> "Report was made that on May 13, 1955, the Special Commission appointed by the Governor of the State of Michigan in the matter of the dispute between the company and the Utility Workers Union of America,

C.I.O., recommended payment by the company of life insurance or death benefits of $1,000 for all retired or retiring employees within the bargaining unit; and that the officers of the company agreed with the union to the payment of death benefits in conformity with the recommendation of the Special Commission. It was further reported that the officers of the company formulated a Death Benefit Plan for all employees of the company, effective March 1, 1955, a copy of which was presented to the meeting. Under the Plan, each full-time regular employee who works to or after his normal retirement date and each such employee retiring under the company's Pension Plan with the consent of the company because of total and permanent disability, will be eligible for the benefit. The benefit payable to the designated payee on the death of an employee retiring on or after March 1, 1955 will be $1,000 or the amount for which he was eligible under an existing group life insurance plan put into effect on July 1, 1944, if greater. The maximum amount payable under the existing insurance plan is $2,000.

Upon motion duly made and seconded, the following resolution thereupon was unanimously adopted:

Resolved: That the Death Benefit Plan for the company's employees in the form submitted to this meeting be and hereby is approved and that the officers of the company be and hereby are authorized to do all things necessary to carry out the Plan.

* * *

I, P. A. Perry, Assistant Secretary of Consumers Power Company, do hereby certify that the foregoing is a true and correct copy of preamble and resolution

duly and regularly adopted at meeting of the board of directors of Consumers Power Company duly held on September 22, 1955, at which a quorum was in attendance and voting throughout and that said preamble and resolution have not since been rescinded but are still in full force and effect.

In Witness Whereof, I have hereunto set my hand and affixed the seal of the Company this 9th day of November, 1965."

The findings and recommendations of the Special Commission, here as Exhibit BB, that had to do with the foregoing resolution by the Company recites the following:

"UNION PROPOSAL NO. 40

(Insurance for Retired Employees)

'The Company to provide $1500 life insurance for each retired and retiring employee.'

We have stated in connection with Union Pension Plan Proposal No. 9 our view that the parties should negotiate life insurance benefits for retired and retiring employees. In our opinion the Company does owe some responsibility in this regard to retired and retiring employees, although less than to employees on the payroll. Because of the cost of insurance for older persons companies which provide life insurance for retiring employees generally do so at a reduced amount. In case of some companies it may be more economical to pay a death benefit directly rather than covering the risk by insurance.

Recommendation

> The Commission recommends that the parties agree to a contract provision whereby the Company provides life insurance or death benefits of $1,000 for all retired or retiring employees."

The Death Benefit Plan itself, here as Exhibit DD, is devoid of any mention of "deferred compensation" and is equally devoid of any writing that would permit an inference from which a conclusion could be drawn that the plan had anything to do with deferred compensation.

We have purposely given defendant's argument (that the plaintiff's Death Benefit Plan encompasses "deferred compensation") extensive exposure because it is difficult for us to understand how the defendant can advance such an argument in view of the absence of testimony, on direct or cross examination, to support such a theory, and in view of the modus operandi of the plan during the taxable years in question. When we add to the foregoing the statement by Judge Arundell of the Tax Court in *John C. Nordt Co., supra*, at page 442, that "[n]either the regulations nor the Code itself purports to answer the question of what constitutes 'a [Death Benefit] plan' under Section 404(a) (5)," we are at a loss to comprehend how the defendant can so easily place it in Section 404(a)(5) as deferred compensation. Section 404(a) (5) must be the catch-all to end all catch-alls.

Defendant readily concedes that plaintiff's Death Benefit Plan is not encompassed by (1), (2), or (3) of Section 404(a). It does not so concede as to Section 404(a) (5). It is the conclusion of the Court, however, that it was not a plan deferring the receipt of compensation and, accord-

ingly, was not a plan limiting the plaintiff to deductions for only the amount of the benefit paid to the beneficiary at the time of actual payment.

In *Commissioner v. Champion Spark Plug Company*, 266 F. 2d 347 (6th Cir. 1959), we find the following:

> "Briefly stated, the salient facts are that the board of directors of the respondent corporate taxpayer adopted a resolution in the latter part of 1953, directing the payment of $33,750 to a totally disabled salesman-employee (or, in the event of his death, to his widow), as a substitute for a policy of insurance on the salesman's life which it had unsuccessfully attempted to secure under a pension plan; and the Tax Court considered that the authorized payment by the corporate taxpayer to its employee was an unconditional obligation to pay a business expense upon the adoption of the resolution by the directors on December 16, 1953. The court considered that the obligation became then 'accrued', as the taxpayer, during 1953, had kept its books and reported its income in compliance with the accrual method of accounting.
>
> The United States Tax Court held that, in the circumstances of the case, the authorized payment to respondent's employee was a deductible business expense for the year 1953, although the sum authorized to be paid was payable to the employee in sixty equal semi-monthly installments, beginning January 15, 1954.
>
> We believe that the tax court reached a correct result, upon the basis of its findings of fact and opinion. Accordingly, its decision is affirmed."

The tax court, in *Champion*, had stated the following:

> "We are convinced that a study of the entire record shows that Badger had been fully paid for past serv-

> ices and the authorized payment was not compensation for any services rendered to the petitioner. It was to alleviate the financial hardship suffered as a result of his fatal illness. Petitioner, with commendable solicitude for the sad plight of a faithful employee, felt some measure of obligation due to the fact that his assigned position had resulted in his loss of insurability. Petitioner's discharge of the obligation in the manner revealed by this record was not the payment of compensation under any plan deferring the receipt of compensation such as to render section 23(p), or the quoted regulations, applicable.* * *" *Champion Spark Plug Co.*, 30 T.C. 295, 300 (1958).

As an alternative theory (alternative to the theory of deferred compensation), the defendant contends:

> That if Section 404(a)(5) did not apply to the plaintiff's Death Benefit Plan and prohibit any deduction before actual payment of the benefit to a retired employee's beneficiary, the plaintiff was not otherwise entitled to deduct any "accrued liability" under the plan;
>
> that Section 461, Internal Revenue Code of 1954, provides that a deduction shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income;*
>
> that for a taxpayer computing its taxable income by the accrual method it has long been held that in order truly to reflect the income of a given year, all the

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* The parties have stipulated that for 1955, 1956 and 1957 the plaintiff filed its corporate tax returns using the accrual method of accounting.

events must occur in that year which fixed the amount, and the fact of the taxpayer's liability for the items of indebtedness deducted though not paid;

that under this funamental principle of tax accounting, a taxpayer may not accrue an expense the amount of which is unsettled or the liability for which is contingent.

In support of this theory defendant relies upon *Dixie Pine Co. v. Commissioner*, 320 U.S. 516, 519 (1944); *United States v. Consolidated Edison Co.*, 366 U.S. 380, 385 (1961); and *Security Flour Mills Co. v. Commissioner*, 321 U.S. 281, 284 (1944). This Court certainly has no quarrel with the legal proposition for which these three opinions stand as it pertains to the facts under consideration by the Supreme Court in each of the three cases. However, the facts in the three cited cases are as foreign to the facts in this case as a fish is to feathers.

> "Decision of the issue presented in these cases must be based ultimately on the application of the fact-finding tribunal's experience with the mainsprings of human conduct to totality of the facts of each case." *Commissioner v. Duberstein*, 363 U.S. 278, 289 (1960).

Continuing with its alternative theory defendant invokes Treasury Regulations on Income Tax (1954 Code), Section 1-461-1 (a)(2) providing that:

> "Under an accrual method of accounting, an expense is deductible for the taxable year in which *all the events* have occurred which determine the fact of the liability and the amount thereof can be determined with reasonable accuracy." (Emphasis supplied.)

and argues that strict adherence to this "all events" test for revenue purposes is necessary "to prevent the permanent exemption of income of a continuing business from payment of tax."

Plaintiff's answer to defendant's "all events" theory is that all the events *had* occurred in each of the taxable years in question to establish the fact of liability to its retired employees, and that the amount of such liability could be determined with reasonable accuracy.

The posture of this aspect of the case is perfectly clear—the defendant contending that a certain test must be met in order to sustain plaintiff's tax theory, and the plaintiff contending that it has fully met the test.

Of assistance to us in arriving at a proper determination of this issue is *United States v. Anderson*, 269 U.S. 422 (1926), in which we find the following at page 441:

> "In a technical legal sense it may be argued that a tax does not accrue until it has been assessed and becomes due; but it is also true that in advance of the assessment of a tax, all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it. * * * "

Peninsular Metal Products Corporation, 37 T.C. 172, 178-179 (1961), concerns a situation where the taxpayer's liability had become "fixed, absolute and unconditional" by virtue of a 1956 agreement, and the Court there held that the "all events" test was satisfied and the taxpayer should prevail. We quote below from this case:

> "Petitioner cites *Champion Spark Plug Co.*, * * * as being a case very closely in point to the issue here involved. * * * In the instant case the respondent, in contending that petitioner is not entitled to deduct any

amount in 1956, argues that the agreement of March 17, 1956, was a *modification* of the prior employment agreement of July 28, 1954. There is no merit in this argument. The agreement of July 28, 1954, was 'terminated for breach, effective immediately' on January 19, 1956, at which time Burgess was removed as president and general manager of the petitioner. Burgess and his attorney protested the discharge of Burgess and the cancellation of his contract. A definite and clear-cut dispute arose between petitioner and Burgess. Petitioner claimed it had discharged Burgess and cancelled his contract because Burgess had been guilty of numerous and serious defaults in the performance of his employment agreement and had breached his employment agreement, all of which was denied by Burgess. In order to settle the controversy amicably, petitioner and Burgess entered into the agreement of March 17, 1956. This agreement was in no way a modification or revision or a continuation of the employment agreement of July 28, 1954, but was a separate, distinct, and definite agreement executed between petitioner and Burgess to settle amicably the controversy which had arisen between them, whereby petitioner became absolutely liable to pay Burgess the then-determined amount of $117,400. The agreement of March 17, 1956, was not subject to any contingencies or conditions. Burgess was not obligated or required to render or perform any services or refrain from doing anything. The liability to Burgess was fixed, absolute, and unconditional whether Burgess lived or died. All the events had occurred in 1956 which determined the fact of petitioner's liability to pay Burgess $117,400 as liquidated damages. We think the instant case is substantially on all fours in principle with *Champion Spark Plug Co., supra.*

> For the reasons previously given we hold that petitioner is entitled to deduct the full amount of $117,400 from its gross income in its income tax return for the year 1956. * * *"

From all the foregoing the Court concludes that when plaintiff issued a Death Benefit Plan Certificate to a retired or retiring employee of the Company during any of the years 1955, 1956 or 1957, then and at that time its liability under the provisions of the Certificate was clearly established; also, the amount of said liability *could* be determined with reasonable accuracy. The plan, therefore, met the "all events" test set forth in Treasury Regulations on Income Tax, 1954 Code, Section 1.461-1(a) (2).

Since plaintiff has conformed to the "all events" requirement of the tax regulations, it is entitled to deduct the face amount of each Death Benefit Plan Certificate issued to a retired* employee of the Company for the year of issuance —1955, 1956 or 1957.

---

* or retiring

JUDGMENT

(Filed June 9, 1969)

The Court having considered the evidence and the arguments of counsel, and having entered its Opinion herein, it is in conformity therewith:

Ordered, That plaintiff have judgment against defendant for the principal amount of $238,378, with interest at six percent according to law on the amount of $47,216 from September 14, 1956, on the amount of $38,532 from June 14, 1957, and on the amount of $152,630 from June 13, 1958.

Done in open court at Detroit, Michigan, this 9th day of June, 1969.

Thomas P. Thornton,
United States District Judge.

* * * * *

JOINT MOTION FOR CORRECTION OF JUDGMENT

(Filed July 11, 1969)

The plaintiff and defendant, without waiving their respective rights to appeal the Court's findings of fact and conclusions of law, jointly move under Rule 60(a), Federal Rules of Civil Procedure, that the judgment entered on June 9, 1969, be corrected by the entry of the corrected judgment which is attached to this motion.

/s/ Clifford H. Domke,
Badgley, Domke, McVicker and Marcoux,
Attorney for Plaintiff.

/s/ Donald R. Anderson
Tax Division
Department of Justice,
Attorney for Defendant.

CORRECTED JUDGMENT

(Filed July 11, 1969)

Upon the joint motion of the parties; the judgment entered on June 9, 1969, is hereby corrected and it is

Ordered that plaintiff have judgment against defendant for the principal amount of $242,122.18 with interest at six percent per annum on the following *amounts* from the following *dates* to a date preceding the date of the refund check by not more than thirty days, such date to be determined by the Commissioner of Internal Revenue or his delegate:

	Amount	*Date*
(1)	$ 35,759.54	September 14, 1956
(2)	354.65	June 14, 1957
(3)	16,245.32	April 29, 1958
(4)	2,713.23	June 4, 1958
(5)	129,756.94	June 13, 1958
(6)	23,009.50	October 10, 1958
(7)	33,971.12	November 16, 1958
(8)	311.88	August 10, 1962

Done in open Court at Detroit, Michigan, this 11th day of July, 1969.

Thomas P. Thornton,
United States District Judge.

Approved as to form, amounts, and dates:

/s/ Clifford H. Domke,
Bagley, Domke, McVicker & Marcoux,
Attorney for Plaintiff.

/s/ Donald R. Anderson,
Tax Division,
Department of Justice,
Attorney for Defendant.

APPENDIX B

DECISION OF COURT OF APPEALS

UNITED STATES COURT OF APPEALS

For the Sixth Circuit

Nos. 19,916, 19,917

Consumers Power Company
Plaintiff-Appellee
v.
United States of America
Defendant-Appellant

Consumers Power Company
Plaintiff, Cross-Appellant
v.
United States of America
Defendant, Cross-Appellee

(Decided June 5, 1970)

Before Combs and Brooks, Circuit Judges, and O'Sullivan, Senior Circuit Judge.

Brooks, Circuit Judge: This appeal involves questions relating to the federal income tax liability of the plaintiff-appellee, Consumers Power Company. Consumers brought suit to recover a portion of the income taxes it paid for the taxable years 1954 through 1957. Two issues are presented on review. First, Consumers argues that it should have been able to deduct from its gross income as ordinary and necessary business expenses payments made to the Electric Companies Advertising Program (ECAP), an organization of privately owned electric power companies, for

a national advertising campaign carried on during the four year period in question. Second, Consumers contends that it was correct in deducting the face amount of certain death benefit certificates it issued to retiring employees in the years in which the certificates were issued rather than in the years when the death benefits were actually paid. The District Court disallowed the deductions for the expenses of the advertising program, but permitted Consumers to deduct the face amount of the death certificates in the years in which they were issued. See 299 F. Supp. 1180 (1969).

The payments Consumers made to the Electric Companies Advertising Program were its pro rata share of the cost of a national advertising campaign. An examination of the materials used show the campaign had a two-fold purpose: 1. explaining how electricity can make for more comfortable living, and 2. pointing out the "bad features" of publicly owned electric power companies as compared to privately owned companies. The advertisements for which the District Court disallowed deductions were the ones which in some way attacked public power. Some of the disallowed advertisements made a hard sell attack on public power calling it "creeping socialism", while others simply suggested that private power companies can provide faster service because, unlike with publicly owned power companies, there was no waiting to have funds appropriated for the needed electrical facilities. Many of the advertisements were directed toward the Tennessee Valley Authority, and several admonished the public to let their congressmen know how they felt about governmental ownership of electric power companies.

The deductibility of the costs of these advertisements is governed by whether it was an "ordinary and necessary" business expense (Title 26 U.S.C. §162). The Internal

Revenue has promulgated 26 C.F.R. §1.162.20(b)[1] in conjunction with the "ordinary and necessary" business expense section of the Code. This regulation has been considered by the courts at various times. See, *Cammarano v. United States*, 358 U.S. 498 (1959); *American Hardware & Equipment Company v. Commissioner of Internal Revenue* 202 F. 2d 126 (4th Cir. 1953); *Roberts Dairy Company v. Commissioner of Internal Revenue*, 195 F.2d 948 (8th Cir. 1952); *Southwestern Electric Power Company v. United States*, 312 F. 2d 437 (Ct. Cl. 1963). And our review of the disallowed advertisements in light of the interpretation given 26 C.F.R. §1.162.20(b) by these cases supports the District Court's determination of nondeductibility. Several of the advertisements are what might be called border line cases for deductibility, but we defer to the District Court's judgment in those cases. However, it should be noted that this regulation, 26 C.F.R. §1.162.20(b), is apparently capable of infinitely encompassing proportions. In a situation similar to the present one, where no legislation is pending,

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[1] (b) Taxable years beginning before January 1, 1963—(1) In general. (i) For taxable years beginning before January 1, 1963, expenditures for lobbying purposes, for the promotion or defeat of legislation, for political campaign purposes . . . . or for carrying on propaganda (including advertising) related to any of the foregoing purposes are not deductible from gross income. For example, the cost of advertising to promote or defeat legislation or to influence the public with respect to the desirability or undesirability of proposed legislation is not deductible as a business expense, even though the legislation may directly affect the taxpayer's business.

* * *

(2) Expenditures for promotion or defeat of legislation. For purposes of this paragraph, expenditures for the promotion or the defeat of legislation include, but shall not be limited to, expenditures for the purpose of attempting to—

(i) Influence members of a legislative body directly, or indirectly by urging or encouraging the public to contact such members for the purpose of proposing, supporting, or opposing legislation, . . .

and a company's chief competitor is governmentally owned, the regulation could possibly be extended to disallow a deduction for the cost of an advertisement which simply conveys a competitive message. It is not inconceivable that the expenitures for this type of advertisement might fall into the disallowed category of expenditures which according to the Internal Revenue "include, but shall not be limited to. . . ." attempts to "influence members of a legislative body . . . indirectly by urging or encouraging the public to contact such members for the purpose of proposing, supporting or opposing legislation." Such type of coercive use of this regulation to discourage private industry from competing in an ordinary business fashion with a publicly owned business would clearly not be in keeping with the intent of the "ordinary and necessary" business expense provision of the Code.

The other question persisted on this appeal is whether Consumers should have been able to deduct the amount of certain death benefit certificates issued to retiring employees in the year the certificates were issued or only in the year the benefits were actually paid. The District Court allowed the deduction in the year in which the certificates were issued. It based its decision in part on the argument that Title 26 U.S.C. §404(a) and (a)(5)[3] would not apply

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[2]. . . if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such . . . compensation shall not be deductible under section 162 or section ~~212~~, but, if they satisfy the conditions of either of such sections they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year.

* * *

(5) In the taxable year when paid, if the plan is not one included in paragraph (1), (2), or (3) (not here involved), if the employee's rights to or derived from such employer's contribution or such compensation are nonforfeitable at the time the . . . compensation is paid.

under these circumstances because Consumers' death plan was not a plan for "deferred compensation". However, 26 C.F.R. §1.404(a)-1 (a)(1) states that "section 404(a) also governs the deductibility of unfunded pensions and death benefits paid directly to former employees or their beneficiaries." In adition, death benefit plans have in the past been classified as compensations. See *New York Post Corporation v. Commissioner of Internal Revenue*, 40 T.C. 882 (1963); *Scavey & Flarsheim Brokerage Company v. Commissioner of Internal Revenue*, 41 B.T.A 198 (1940). Our examination of Consumers' death benefit plan, and the circumstances surrounding its establishment, leads us to the conclusion that it was a program of deferred compensation for services rendered. Thus, Title 26 U.S.C. 404(a) controls and Consumers can only deduct the amount of death benefits paid under its plan in the years in which the payments are actually made.

Affirmed in part, *reversed* in part.

APPENDIX C

STATUTES INVOLVED

United States Code, Title 26

1. Before Tax Reform Act of 1969:

Sec. 404(a)

"(a) General Rule. If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under section 162 (relating to trade or business expenses) or section 212 (relating to expenses for the production of income); but, if they satisfy the conditions of either of such sections, they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year:

* * * * *

"(5) Other Plans. In the taxable year when paid, if the plan is not one included in paragraph (1), (2), or (3), if the employees' rights to or derived from such employer's contribution or such compensation are nonforfeitable at the time the contribution or compensation is paid."

2. After Tax Reform Act of 1969:

Sec. 404(a)

"(a) General Rule. If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is

paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under section 162 (relating to trade or business expenses) or section 212 (relating to expenses for the production of income); but, if they satisfy the conditions of either of such sections, they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year:

* * * * *

"(5) Other Plans. If the plan is not one included in paragraph (1), (2), or (3), in the taxable year in which an amount attributable to the contribution is includible in the gross income of employees participating in the plan, but, in the case of a plan in which more than one employee participates only if separate accounts are maintained for each employee."

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SUPREME COURT, U. S.

No. 448

In the Supreme Court of the United States

October Term, 1970

CONSUMERS POWER COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,
JOSEPH M. WAFFEN,
Assistant Attorney General,
WILLIAM A. FRIEDLANDER,
RICHARD W. PERRIN,
Attorneys,
Department of Justice,
Washington, D.C. 20530

In the Supreme Court of the United States

OCTOBER TERM, 1970

No. 619

CONSUMERS POWER COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the district court is reported at 299 F. Supp. 1180 (Pet. App. 7–23). The opinion of the court of appeals is reported at 427 F. 2d 78 (Pet. App. 26–30).

JURISDICTION

The judgment of the court of appeals was entered on June 5, 1970. A petition for rehearing was denied on July 6, 1970. The petition for a writ of certiorari was filed on August 31, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

407-291—70

QUESTION PRESENTED

Whether petitioner's death benefit plan was a plan deferring the receipt of compensation within the meaning of Section 404(a)(5) of the Internal Revenue Code, so that the deductions allowable to petitioner under that plan are limited to the payments actually made.

STATUTES AND REGULATIONS INVOLVED

Pertinent statutory provisions are set forth in Appendix C to the petition (Pet. App. 31–32). Pertinent Treasury Regulations on Income Tax (1954 Code) are set forth in the Appendix, *infra*, pp. 7–8.

STATEMENT

In March, 1955, petitioner experienced a labor dispute with its union employees. To help settle the dispute, petitioner agreed in writing to provide, at retirement, life insurance or the right to death benefits of $1,000, to all employees who worked for petitioner until their retirement date. (R. 36a–37a.)[1] In September, 1955, pursuant to that agreement, petitioner's board of directors approved a death benefit plan for all full-time regular employees (R. 37a, 987e), which remained in effect through 1955, 1956 and 1957, the years here in suit (R. 37a). As employees entitled to death benefits under the plan retired, each was given a death benefit certificate evidencing petitioner's obligation to pay his beneficiaries $1,000 upon his death (R. 38a, 1034e). During the years in suit, petitioner

[1] "R." references are to the separately bound record appendix filed in the court below.

delivered 240 such certificates and claimed a deduction of $239,800 for the face amount thereof (R. 38a), without regard to the amounts actually paid thereunder.

The government contended that the death benefits constituted deferred compensation within the coverage of Section 404(a) of the Internal Revenue Code, and that deductions were therefore allowable, as provided by Section 404(a)(5), only in the amount actually paid out pursuant to the certificates. The district court rejected the government's contention (Pet. App. 23), and the court of appeals reversed (Pet. App. 26–30).

ARGUMENT

The decision below is correct. There is no conflict of decisions or any other ground for further review.

1. Section 404(a) provides in general that accrued liability to pay compensation under deferred payment plans which satisfy other requirements of the Internal Revenue Code shall be deductible subject to the limitations of Section 404. As applicable to the years in suit, Section 404(a)(5) permits deductions under plans of the type here involved only "[i]n the taxable year when [compensation is] paid." See *New York Seven-up Bottling Co.* v. *Commissioner*, 50 T.C. 391; *New York Post Corp.* v. *Commissioner*, 40 T.C. 882; *Seavey & Flarsheim Brokerage Co.* v. *Commissioner*, 41 B.T.A. 198.

Petitioner does not directly question the reasoning by which the court below concluded that its death benefit plan constituted deferred compensation and

therefore was covered by Section 404(a). Rather, it suggests (Pet. 4, 5) that the result reached by the court of appeals represents an unwarranted judicial erosion of accrual accounting principles. But the court below (and the others which have reached the same result) did not overlook the general rules of accrual accounting to which petitioner refers. It construed Section 404(a) as an express legislative exception to those rules for death benefit plans. There can be no doubt that Congress has the authority to create such an exception, and that it did so in Section 404(a). Petitioner's reliance on the general rules thus is misplaced.

2. Petitioner also argues (Pet. 5–6) that amendments to Section 404(a)(5) made by the Tax Reform Act of 1969, P.L. 91–172, 83 Stat. 487, Section 321(b)(3), would entirely deny petitioner a deduction for benefits paid under its death benefit plan. From this premise, petitioner seeks to draw the conclusion that Congress never intended that Section 404(a)(5) should apply to such death benefit plans (Pet. 6). This argument assumes, with no support in the legislative history of the recent amendment to Section 404(a), that the 91st Congress gave some specific consideration to the deductibility of accruals under death benefit plans, or to the coverage *vel non* of such plans under Section 404(a) in pre-1969 years.[2]

[2] This Court has questioned the weight to be given to the views of a later Congress as to the proper construction of a measure enacted by an earlier Congress. See, *e.g.*, *United States* v. *Price*, 361 U.S. 304, 313.

Whether the new language of Section 404(a)(5), which limits deductions to amounts includible in the gross income of employees, will be judicially—or even administratively—construed and applied so as to have the effect asserted by petitioner remains to be determined.[3] At all events, that language is irrelevant with respect to taxable years—including those here in issue—which preceded the effective date of the amendments to Section 404(a)(5).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.
JOHNNIE M. WALTERS,
Assistant Attorney General.
WILLIAM A. FRIEDLANDER,
RICHARD W. PERKINS,
Attorneys.

OCTOBER 1970.

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[3] The issue is presently under study by the Treasury Department.

APPENDIX

Treasury Regulations on Income Tax (1954 Code) (26 C.F.R.):

§ 1.404(a)–1 *Contributions of an employer to an employees' trust or annuity plan and compensation under a deferred payment plan; general rule.*

(a)(1) Section 404(a) prescribes limitations upon deductions for amounts contributed by an employer under a pension, annuity, stock bonus, or profit-sharing plan, or under any plan of deferred compensation. It is immaterial whether the plan covers present employees only, or present and former employees, or only former employees. Section 404(a) also governs the deductibility of unfunded pensions and death benefits paid directly to former employees or their beneficiaries (see § 1.404(a)–12). For taxable years beginning after 1962, certain self-employed individuals may be covered by pension, annuity, or profit-sharing plans. For the rules relating to the deduction of contributions on behalf of such individuals, see paragraph (a)(2) of § 1.404(a)–8 and § 1.404(e)–1.

* * * * * *

§ 1.404(a)–12 *Contributions of an employer under a plan that does not meet the requirements of section 401(a); application of section 404(a)(5).*

Section 404(a)(5) covers all cases for which deductions are allowable under section 404(a) but not allowable under paragraph (1), (2), 3), (4), or (7) of such section. No deduction is allowable under section 404(a)(5) for any contribution paid or accrued by an employer under